Exhibit Z 11 pg 1

Investment News: Money Morning

Investment News Provider

White House Approves $13.4 Billion in Loans for GM and Chrysler

By Jason Simpkins
Associate Editor
Money Morning

General Motors Corp. (GM) and Chrysler LLC will receive $13.4 billion in loans from the federal government as part of an emergency measure to keep the companies operating at least until the spring.

"These are not ordinary circumstances, in the midst of a financial crisis and a recession allowing the U.S. auto industry to collapse is not a responsible action," said President Bush, who made the final decision to move ahead with the bailout after Senate Republicans last week balked at passing a House-approved rescue of the auto companies.

"Chapter 11 is unlikely to work for the American automakers at this time," he added.

The $13.4 billion will be taken from the Troubled Asset Relief Program (TARP). GM and Chrysler will then get an additional $4 billion in February.

However, both companies are being forced to accept a number of conditions that include limiting executive pay, reducing debt obligations, and striking new agreements with the United Auto Workers union that bring employee wages and benefits down to levels that are more competitive with those of foreign-based automakers working in the United States.

The companies will also provide the government with warrants for non-voting stock, and federal officials will examine all of the companies' financial statements. The government has the authority to block any transaction of $100 million or more.

The government's debt will have priority over all other debts, and if the two automakers fail to demonstrate financial viability by March 31, the loans will be called and the money returned. That's a tall order for GM and Chrysler, which are faced with plummeting sales and a harsh economic

Exhibit Z11 pg2

environment.

GM, the nation's largest automaker, has suffered roughly $73 billion in losses since 2004, and its U.S. sales are down 22% this year, ***Bloomberg News*** reported. The company said earlier this month that light vehicle sales plunged 41% in November, dropping to 153,404 vehicles from 261,273 during the same month a year ago.

Chrysler sales were off 47% last month and down 28% through the first 11 months of the year. The company yesterday (Thursday) announced that it would close all 30 of its North American manufacturing plants for four weeks. GM followed suit temporarily closing 20 factories.

"I've been in this business since the time of Lee Iacocca and all the bad times we went through in the 1980s were nothing compared to this," Tim Finegan, owner of a Chysler dealership told ***The Associated Press***. "But for now, our lights are still on and our bills are paid, so you just show up every morning and say maybe today will be a little better."

News and Related Story Links:

- **Bloomberg:**
  GM and Chrysler Will Get $13.4 Billion in U.S. Loans
- **Money Morning:**
  Big Three to Shutter 59 Plants – Chrysler Forces Dealers to Sell at a Loss
- **Money Morning:**
  White House Opens TARP to Auto Industry after Congress Fails to Approve Loans
- **The Associated Press:**
  Plant shutdowns give autoworkers holiday blues

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More on this topic (What's this?)

The future for US Auto Stocks (Dividend Growth Investor, 11/11/08)

Jones Day's Chrysler Charge To Taxpayers: $12,702,190.19 (Zero Hedge, 7/19/09)

The Value Of Detroit Fuel Economy (Green Chip Stocks, 6/23/09)

GM Dissident Bondholders File Objection To 363 Sale (Zero Hedge, 6/19/09)

Read more on **General Motors**, **Chrysler**, **Auto Makers** at **Wikinvest**

December 19th, 2008

Exhibit 19
Part 2

Source: Continuous Improvement Associates
http://www.exponentialimprovement.com/cms/fallacy.shtml

Social Issues

The Trade Deficit and the Fallacy of Composition

By Bob Powell, 5/04/05

Use your browser to search for "Updated". Especially see the chart on when the GDP crosses the cumulative trade deficit in the "What's Happening" section below.

Go to the section describing the "Fallacy of Composition"

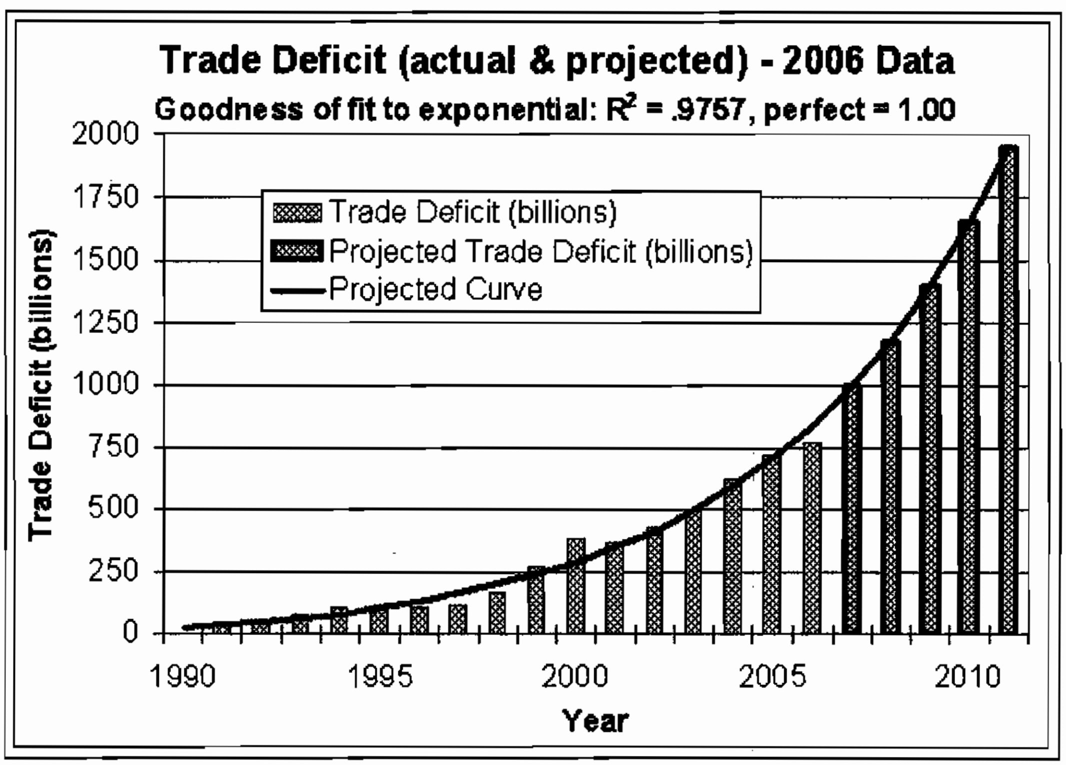
A presentation, "The Problem is Bigger than the Loss of Manufacturing" (Powerpoint, 1280K, links active in SlideShow mode, PDF w/links, 471K, PDF w/notes, 433K: Updated and expanded 8/28/07), contains updated charts on the U.S. 'trade' deficit and Colorado jobs through of July 2007 plus a summary of the main points on what to do about 'trade', taxes, and health insurance.

See also the very short handout on The Coming Economic Collapse from 'Trade' and Offshoring. 7/17/07.

Preface. The Impact of an Exponentially-Increasing Trade Deficit: We're Between a Rock and a Hard Place

The U.S. economy will collapse. Repeat. The U.S. economy, and probably the world economy, will collapse because of the United States' exponentially-increasing trade deficit.

Updated chart:



Trade Deficit thru 2006 with Trend: An excellent fit to an exponential function. Perfect fit = 1.000

That's overall and it's increasing rapidly with China, too. See the chart below.

The rest of the world will, within the next few years if not sooner (it's already happening), decide to stop taking U.S. dollars

for their goods. As in Iraq, there are no good choices, only bad choices, remaining.

The Rock: The Federal Reserve Doesn't Raise Interest Rates

If the Federal Reserve doesn't raise interest rates to maintain the U.S.'s ability to attract funds to maintain borrowing, it will not be able to finance its trade and fiscal deficits. Not raising interest rates will allow the dollar to fall relative to other currencies and cause inflation as the prices of imported goods rise because the US dollar is worth less.

This will be good for U.S. exports to some extent, but it takes a long time to renew an ability to manufacture goods we no longer produce. This is described by Louis Uchitelle in the New York Times on 12/24/06: Goodbye, Production (and Maybe Innovation) ... it's NOT a "maybe."

A sharp rise in prices (inflation) will over the short term be economically devastating. The economy is now greatly supported by consumer spending, which will be severely impacted by sharply increased prices, especially as the housing bubble, which has allowed many to borrow against home equity and maintain spending, is collapsing.

The U.S. economy will collapse.

The Hard Place: The Federal Reserve Raises Interest Rates

If the Federal Reserve raises interest rates significantly, it will slow the economy. Many consumers will be unable to maintain large and growing consumer debt and bankruptcies will rise. Many more homeowners with variable rate mortgages will face foreclosure. Less consumer spending and higher interest rates will lead to less business activity and associated layoffs.

The U.S. economy will collapse.

Selling Off America

As the trade deficit grows, the U.S. has been selling companies, buildings, ports, and toll roads to take back some of the dollars from foreign hands to stave off the collapse of the dollar. For information on what's been sold, see Economy In Crisis.

What happens? The profits from these enterprises are not retained in the U.S. They are not recirculated in the U.S. (economic multipliers are reduced), which leads to less economic activity. See How a Regional Economy Works.

This growing trade deficit is the root of the controversy over selling U.S. ports to a UAE company. That wasn't, and still isn't, about "good foreign direct investment in the U.S."

Updated 7/27/07: The U.S. has done so much of this that the Bureau of Economic Analysis reports that U.S. net international investment at the end of 2006 was -$2.54 trillion: the amount by which foreign investments in the U.S. exceeds the value of U.S. investments abroad. That's about 45% of the accumulated "trade deficit" ($5.7 trillion in 2006) ... that's a lot of "investing." But substitute "selling off America" for "investing" to better describe what's happening.

By 2014 the U.S. would have to use its entire annual output to retrieve the dollars in foreign hands and buy back the companies, roads, and ports sold to those in other countries.

(See Buffett's chart below showing increasing foreign holdings of U.S. assets.)

A Systems Thinking Perspective on "Trade," Offshoring, & The Fallacy of Composition

This page covers:

- Trade Data and Trends

- The Fallacy of Composition
- Trade Dynamics

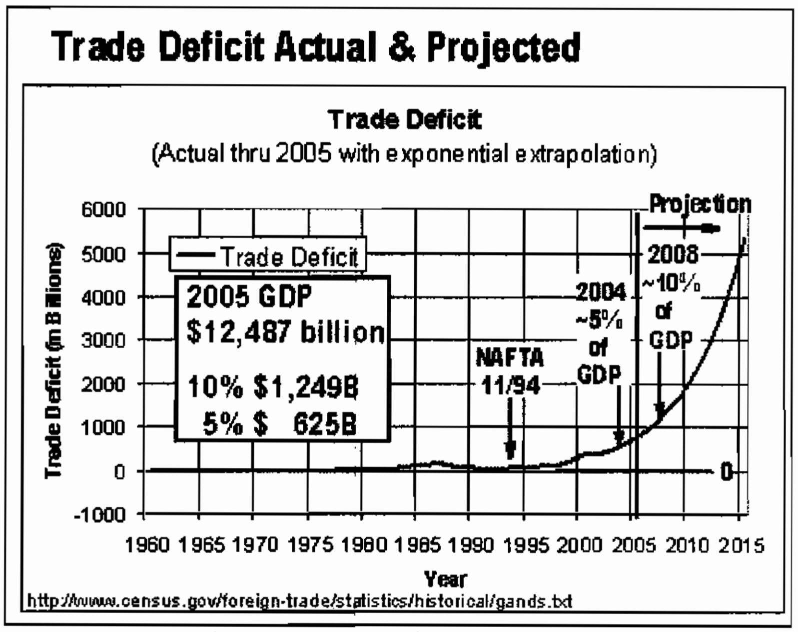
A preliminary on the greatly misunderstood concept of "comparative advantage"

It must be noted that the issue of "trade" and the "trade deficit" is about more than simple "trade." "Trade" is the "exchange of one thing for another," not the "transfer of the factors of production." Because of this, the logic of "comparative advantage" does not apply. This is an important point because "free trade" advocates rest their arguments on the premise that "comparative advantage" applies. It does not. Instead, "absolute advantage" applies.

In A Systems Thinking Perspective on Manufacturing & Trade Policy, I draw from the following sources to explain.

Lester Thurow in *The Future of Capitalism* (1996, pp. 69, 70) explains the "theory of comparative advantage" and describes the assumptions required for it to hold:

> "The classical theory of comparative advantage is often taught as if everyone benefits from trade. Technically that is not true. The total income of every country that takes advantage of comparative advantage grows, but there will be individuals within each country who lose. What the theory holds is that those who gain from international trade receive enough extra income from their activities that they could compensate those who lose when international trade commences. If that compensation isn't actually paid (and it almost never is), then those who lose are quite rational to oppose international trade.
>
> "But in the classical theory the losses usually will be quite small. First, full employment is assumed to exist. Free trade does not push anyone into unemployment. Second, transition costs are assumed to be zero. There is no region-, industry-, or firm-specific physical or human capital that is destroyed when workers are forced to shift between regions, industries, or firms. Third, returns are assumed to be everywhere equal. Each industry has the same rate of return on human or physical capital. Each firm and industry pays the same wage rate for a worker's being willing to give up an hour of leisure. As a consequence, being forced to shift jobs doesn't change wages very much, if at all."



U.S. Trade Deficit - actual with exponential projection

Paul Craig Roberts notes:

> "David Ricardo discovered the principle of comparative advantage in the early 19th century. He recognized that the principle did not hold if all factors of production are internationally mobile. Mobile factors of production would migrate to countries that had the greatest absolute advantages. Those countries would gain and all others would lose. ... Today, absolute advantage resides in an abundant supply of cheap and willing labor."

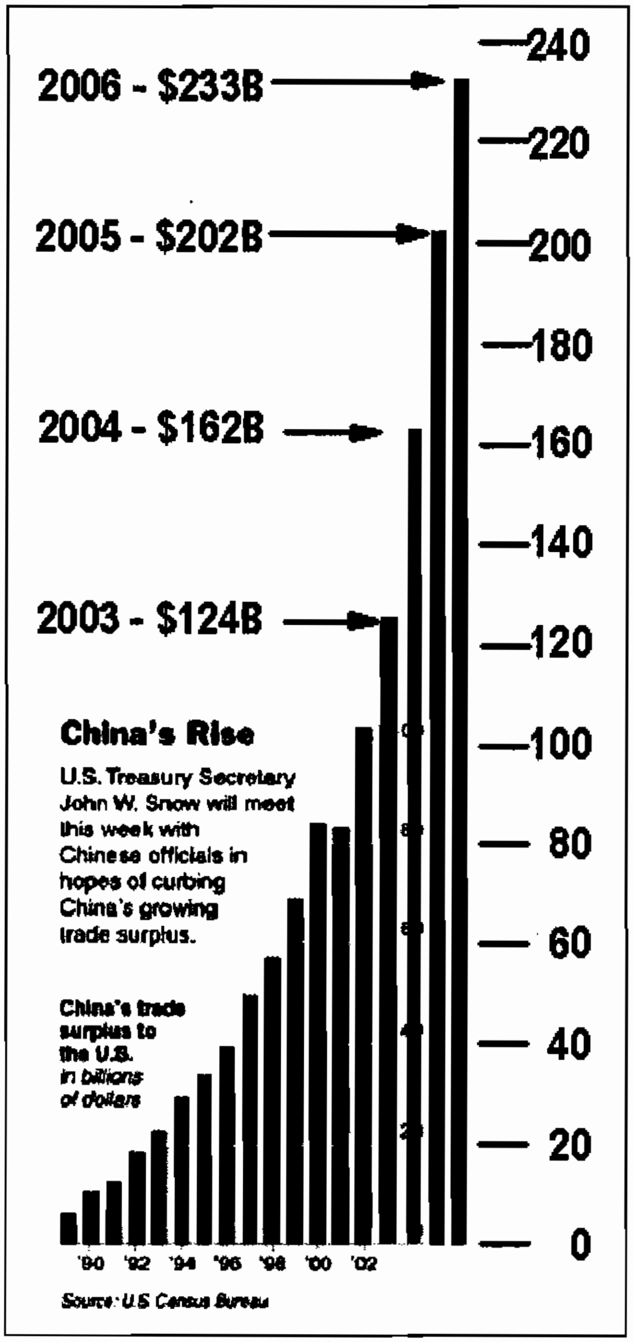
What's happening?

The chart above shows that the trade deficit for 2004, stated as $617.7B, was over 5% of GDP. At that time, projecting along the exponentially-increasing trend (note the confidence in the trend being exponential based on the data was excellent: R-squared = 0.9685), the trade deficit was projected to be at 10% of GDP by 2008.

In line with this trend, the February 2005 deficit was $61.04B, a yearly rate of $732.5B, over 6% of GDP. The actual U.S. trade deficit for all of 2005 was right in line with the exponential trend at $723.6 billion.

A New York Times article [Joseph Kahn, "China Seen Ready to Conciliate U.S. on Trade and Jobs," 9/02/03] described how, in early September 2003, U.S. Treasury Secretary met with Chinese officials in hopes of curbing China's growing trade surplus [... see the black bars in the figure], which was $103B in 2002.

Want to know how that worked out? See the red bars in the figure. The trade deficit in 2005 with China alone was $202B up 25% from 2004's $162B, which was up over 30% from 2003, which was up over 20% from 2002.

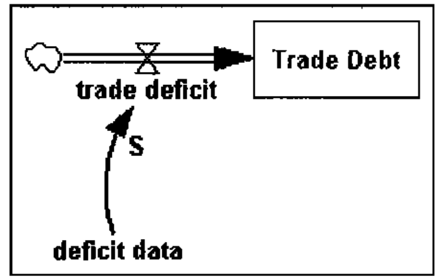


China's rising trade surplus with the U.S.

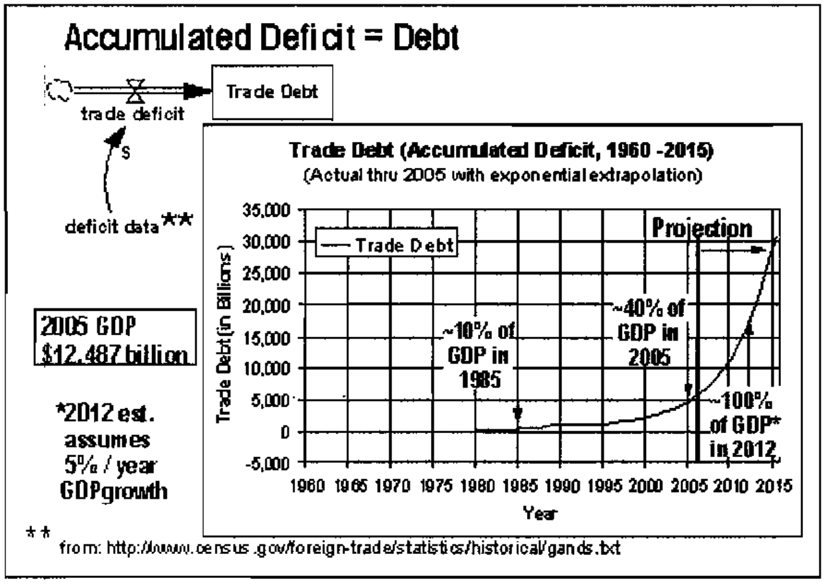
The accumulated trade deficit is was 40% of GDP in 2005. Best fit projections indicated it would be at ~50% of GDP in 2007 and at ~100% of GDP in 2012 (assuming 5% GDP growth from 2005 on).

To me, and many others, this appears to be a serious problem. It's a lot of money to be borrowed from the world. Nothing increases exponentially forever. What

can't go on forever will stop; in this case it will stop when the rest of the world decides to stop taking U.S. dollars for their goods.



Accumulated Deficit = Debt ... an outflow associated with selling U.S. assets could be shown

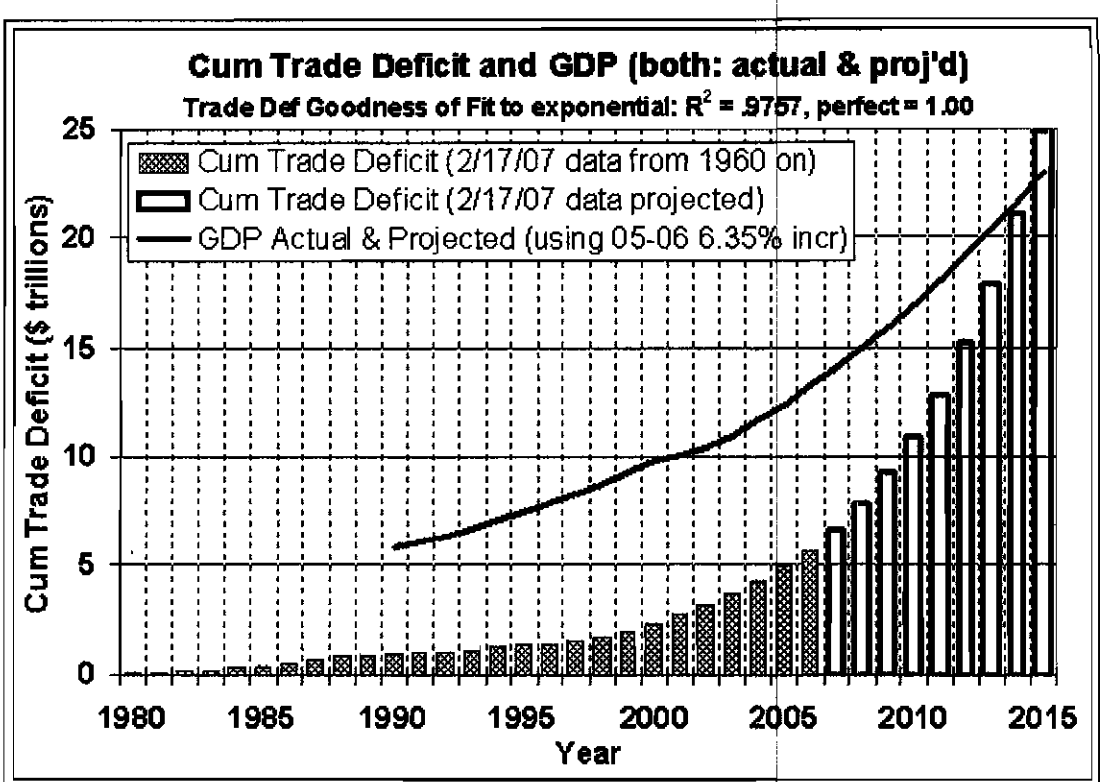


U.S. Trade Debt (Cumulative Deficit) - projection based on the exponential increase shown in the first figure above

Update 7/27/07:

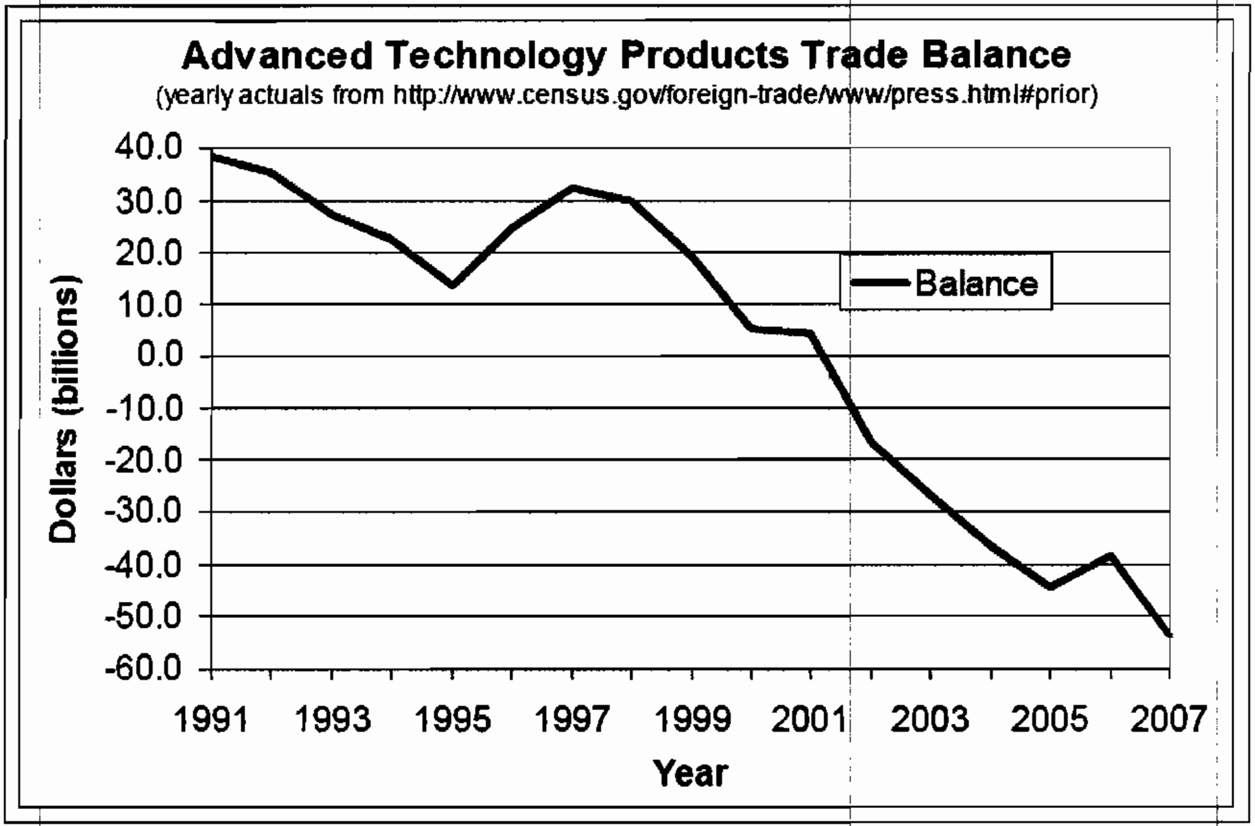
See the chart below. While the 2007 numbers aren't in, the accumulated trade deficit for 2007 is still projected to be 50% of GDP. The current projection is that it will be at 100% of GDP by 2014, instead of 2012. For some reason the U.S. Census Bureau, Foreign Trade Division, sometime between 11-Mar-05 and 8-Jun-07, lowered the 2005 trade deficit by $9,245B (now $714.4B instead of $723.6B) and lowered 2004 by $5B. That makes about a 2 year difference in the projection.

This chart gives a visual picture of the economic forces developing. As is the case for earthquakes, no one knows exactly, or even approximately, when things will give; one only knows it's inevitable.

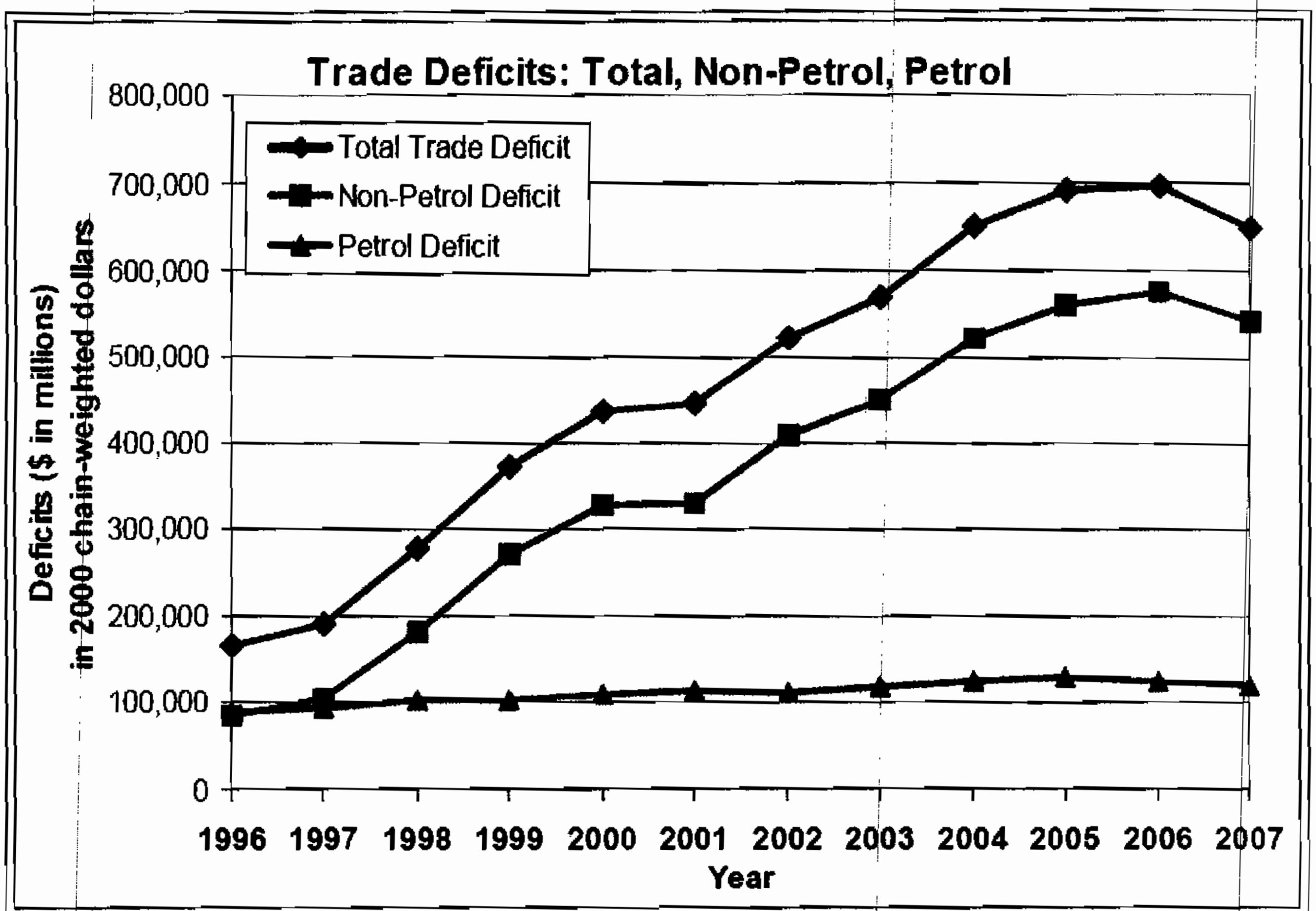


At current trends Cumulative Trade Deficit will equal GDP by 2014, but current trends won't continue. The economy will collapse well before that.

Some say the U.S. should just move up the technology chain and concentrate on high tech products, letting others do the manufacturing and lower tech work. Unfortunately, there is no magic wall between the manufacturing and engineering & design jobs. We're losing high-level jobs, too. See the growing trade deficit in Advanced Technology Products below (data from here, but you have to extract the numbers from multiple files). Updated 7/14/08.



Over the last 16 years, so-called "trade" in Advanced Technology Products has gone from a $38.4B surplus in 1991 to a $53.5B deficit in 2007



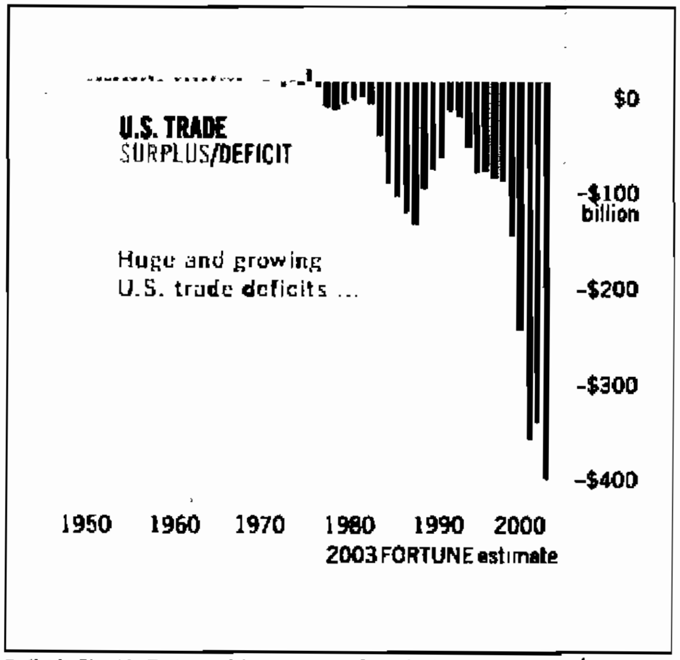
Until I saw a chart like this one, thanks to my friend Dave Anderson, I'd thought the increasing deficit was at least somewhat driven by increasing oil imports. Clearly, that's not what's driving the increases. It's offshoring.

A second preliminary on what to do about it

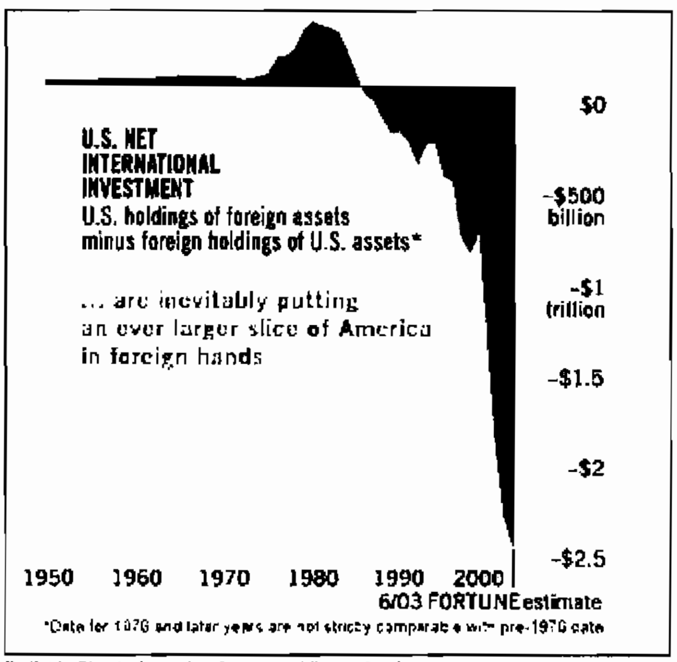
There are so many factors affecting trade that achieving a "level playing field" is extremely difficult. Therefore, focus on outcomes by promoting "even trade" or "balanced trade," not "free trade."

Warren Buffett is also concerned with the long-term problems caused by international trade that's "out of balance." He described the problem and what to do in his article in Fortune: America's Growing Trade Deficit Is Selling the Nation Out From Under Us. Here's a Way to Fix the Problem - And We Need to Do It Now (This link to the original Fortune article no longer gets me there ... so it's also available here).

Below are his charts from that article on the growing trade deficit and growing foreign holdings of U.S. assets. The growing foreign holdings are a result of those holding an increasing quantity of dollars wanting to hold real assets instead. As he says, this indicates we're selling off America as noted above.



Buffett's Chart in Fortune of the growing U.S. trade deficit



Buffett's Chart of growing foreign holdings of U.S. assets

To deal with this out of control situation, he's proposed an Import Certificates mechanism to create balanced trade to deal with what he describes as "a shifting maze of punitive tariffs, export subsidies, quotas, dollar-locked currencies, and the like."

Buffett's Import Certificates mechanism: If a country purchase products or services from the U.S., then it can sell that amount back to the U.S. If it does not want to sell to the U.S., it can sell its Import Certificates to another country that does want to sell to the U.S.

This is a market-based mechanism that would produce **the desired outcome: balanced trade**. This is necessary because anything out of balance will be, WILL BE, brought back into balance. The more out of balance it's allowed to become, the more severe will be the correction.

I would phase in this policy over a decade or so to mitigate the economic shock. Going "cold turkey" would be ugly; "warm turkey" will be painful, but less so than "cold turkey" and much less than will be the consequences of current policies.

To those who want to continue current policies, one might ask, "Why do you hate America?"

The Fallacy of Composition and structures responsible for what's happening

To understand what's happening we need to use systems thinking, which is seeking to understand system behavior by examining "the whole," instead of by analyzing the parts.

A key systems principle is that behavior is a result of structure. So when we see exponential growth, we know reinforcing feedback is driving it. Therefore, we want to identify the feedback structure that's responsible. The causal loop structure is shown below and in the presentation slides. When we understand structure, we can understand behavior and design policies to improve behavior.

Unfortunately, human thinking is subject to the **Fallacy of Composition:** When we act as if what is true for a part is true for the whole. In other words, there are times when individually logical actions are collectively irrational.

To illustrate examples of this fallacy and how system structure determines behavior review three structures:

- Spectator view of the field
- Ocean fishing
- Offshoring

Spectators: When a spectator can't see as well as he'd like, he may stand to improve his view. It does, but it also blocks the view of others. They also stand to get a better view. However, when everyone's standing no one can see better than before. Also, the system is less efficient, because standing takes more energy than sitting. In systems thinking, this is called a "fix that fails."

Ocean Fishing: Consider ocean fishing. Every fisherman logically puts out more boats to increase profits. The additional profits provide funds for even more boats and fishing. But as total fishing approaches the sustainable ocean fishing capacity, the effort required per fish caught increases, which reduces profits because all are less efficient. In systems thinking, this is called a "tragedy of the commons," where the commons is the stock of ocean fish. The spectator example above could also be cast as a "tragedy of the commons," where the commons is the shared view of the field.

There's a perverse additional effect for ocean fishing, because scarcity drives up price, sending exactly the wrong signal to preserve the resource. Many think that market mechanisms always provide appropriate corrections to do what's best for society. This extreme market failure illustrates that this is not true. Another example: Farm Policy Failure.

Offshoring: Let's return to the issue of offshoring and the exponentially increasing trade deficit. When we observe exponential growth we know a reinforcing feedback is responsible. What is it?

The Environment

The world economy is operating in an environment of oversupply compared to demand due to a global glut of economic capacity. This results in extreme price competition and downward pressure on corporate profits (see references below).

The world economy is also operating in a context of an excess of offshore labor supply compared to demand, which produces very low offshore pay. Corporations have found they can tap this low-cost labor supply to increase profits. Each corporation, if it considers profits too low (and corporations logically always want higher profits, no matter what their level), can logically increase offshoring to reduce costs and increase profits.

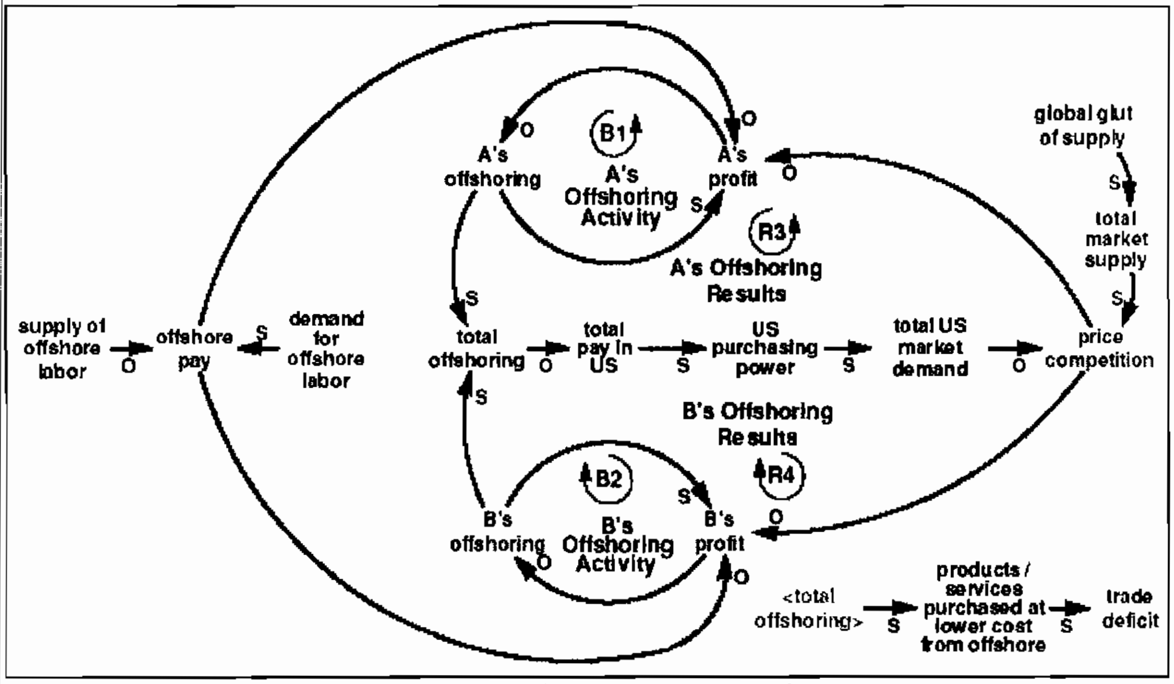
The Logical Logic that's Irrational

Each company's offshoring adds to total offshoring, which also has the effect of lowering pay in the U.S. (see references

below). This in turn reduces U.S. purchasing power and total U.S. market demand, which increases price competition ... leading to pressure for even more offshoring.

So every company logically offshores to cut costs, but when all do, none have lower costs than others and they are no better off than before in competing in the U.S., the world's largest and most profitable market ... for the time being, until we finally kill off the goose that laid the golden eggs.

In addition, U.S. purchasing power erodes, undermining the whole. As long as offshore pay is lower than in the U.S. and there's a global glut of capacity, the individually logical decisions on the part of corporations will power this "reinforcing feedback." Offshoring increases products & services purchased from offshore and in turn results in an exponentially-increasing trade deficit.



The Structure of Offshoring driving an exponentially-increasing trade deficit

Eventually, as offshoring continues, demand for offshore labor will increase, but there will be a long delay before demand for offshore labor exceeds supply. This will keep offshore wages low for decades, if not a century. If there were to be a world equilibrium of pay, one might expect the equilibrium would be at the weighted mean between U.S. and China pay. Because there are so many Chinese workers compared to U.S. workers and because their pay is so low, the equilibrium would be a very low pay indeed.

Some maintain that as economic conditions improve offshore and pay rises, the world will purchase more goods from the U.S. This won't be true because pay will only rise very slowly and they will also purchase from low-cost sources, not from the U.S.

See how the American Chamber of Commerce and World Bank are opposing an increase in working conditions and pay in China at Are there government & business entities that oppose improving working conditions and wages?

Long before we reach such equilibria, the U.S. economy will collapse due to the exponentially-increasing trade deficit as the rest of the world decides to stop taking U.S. dollars for their goods. In response the Federal Reserve will have to raise interest rates to maintain borrowing, because large and growing government deficits and debt won't allow the U.S. to pay off the loans.

This growing trade deficit is the root of the controversy over selling US ports to a UAE company. That wasn't, and still isn't, about "good foreign direct investment in the U.S." (see Buffett's chart above showing increasing foreign holdings of U.S. assets). It's about selling off parts of the US economy (including companies, buildings and toll roads) to take back some of

the dollars from foreign hands to stave off the collapse of the dollar.

Summary:

- This reinforcing feedback will continue long as
    - there's a global glut of supply relative to demand
    - large US-offshore wage disparities exist
    - the US economy doesn't collapse ... exponential increases are unsustainable
- What's individually logical can be collectively irrational.
- Note: the issue of "trade" and the "trade deficit" is about more than simple "trade." "Trade" is the "exchange of one thing for another," not the "transfer of the factors of production." Because of this, the logic of "comparative advantage" does not apply.
- Note: Nations don't "trade" ... companies do. It's not their job to look out for the good of the nation; that's government's job. It's not doing it.
- Exponential growth is slow at first ... lots of frogs are being boiled ... for now! ... because the trade deficit had been rising relatively slowly As the rate of trade deficit growth increases, there will be fewer and fewer boiled frogs; they'll be getting more and more concerned and "jumping out of the pot."
- What to do? See the section above and:
    - **A Systems Thinking Perspective on Manufacturing & Trade Policy**
    - **Why Offshoring is Economically Unsustainable**
    - **How the U.S. Subsidizes Offshoring of Jobs**
    - **American Manufacturing Trade Action Coalition** site.

Note, 10/30/05:

I brought this page to the attention of a "free trade" advocate's comment at The Future of American Manufacturing. He'd written: But what on earth is an economist doing asking "What will be our competitive advantages in the emerging global economy?"?

I noted that Trade and globalization depend upon absolute, not competitive or comparative, advantage, a very different idea. (Sorry I've had a typo above since I wrote this, saying "depend on comparative", when what I actually wrote below was "absolute".) I referred him to this page.

His response:

> I know what the Tragedy of the Commons is. I've written on the subject a number of times myself. You equate offshoring with that. Sorry, TotC is about the overuse of a scare resource because of perverse incentives. Offshoring?? That looks like the use of a different resource for entirely sensible incentives. Don't see, unless you are an economic nationalist, how the two can be compared.

My response:

> To see how they're related, see the slides in my presentation at a meeting of the Colorado Springs Manufacturing Task Force: **A Systems Thinking Perspective on "Trade"** (pdf, 290K). **All** (this "All" version has the cartoons and the page numbers below are for this file). These structures make explicit how the dynamics play out.
>
> The structure on p. 12 is the Tragedy of the Commons applied to ocean fishing, with which you indicate you're familiar. The problem comes about, not because the incentives in this structure are "perverse" for the individual, they are totally logical and produce the desired results until the scarce resource limit is reached ... then comes the tragedy. In systems our problems are often the result of our successes, not our failures.
>
> The figures from pages 13 to 17 build the structure of offshoring. The titles of the slides explain what's going on as the links are added.
>
> You are correct in that they are different structures ... note that reinforcing (R) and balancing (B) loops are interchanged. However, as long as there's low offshore pay and price competition driven by a global glut of

capacity, the reinforcing feedbacks power offshoring and an increasing trade deficit. Reinforcing feedbacks produce exponential behavior ... as shown in one of the figures, the fit of trade deficit numbers to an exponential function is quite good.

What these structures have in common is that, though they are different, they are examples of the fallacy of composition: individually logical decisions producing results that are collectively irrational. That's the comparison; it's not that the structures are the same.

For a guide to Reading Systems Diagrams there's a link to A Brief Introduction to Systems Diagrams that explains the S and O links.

As to whether I'm an "economic nationalist" or not: If there's a choice between being an "economic nationalist" and standing by as our economy crumbles, I'll choose being an "economic nationalist." As I note in my post, I recommend ending "reverse protectionism" and adopting Buffett's balanced trade mechanism ... and we need to end "comparative advantage" arguments that don't apply to the current situation (... absolute advantage is operative).

References on Global Glut of Supply:

The Chicago Tribune, four-part series: "The economics of glut."
December 15, 2002 through December 18, 2002 at: http://www.chicagotribune.com/business/chi-021215glut,1,4874700.storygallery?coll=chi%2Dnewsspecials%2Dhed

Overcapacity Stalls New Jobs By LOUIS UCHITELLE, NY Times, October 19, 2003
http://www.nytimes.com/2003/10/19/business/19SOAP.html

References on Wages:

"Using official Bureau of Labor statistics, Johns Hopkins University economist Arnold Packer calculates that employees' share of the value added in the U.S. economy has fallen to its lowest point since records were first kept in 1947 -- and the rate of decline is accelerating."

> "Maybe We Could All Deliver Pizza . . .,"
> Jodie T. Allen, 3/06/04, The Washington Post,
> http://www.washingtonpost.com/wp-dyn/articles/A35469-2004Mar6.html

The recession in the U.S. has been over for more than three years. The economy has been growing at better than a 4% annual clip for the past two. Profits, at least until recently, have been up. Growth in worker productivity has remained strong. ... Yet wages for the typical worker aren't even keeping up with inflation. Wages are growing unusually slowly for this point in the economic cycle, especially given persistently strong growth in productivity ...

> Workers' Wages Trail Growth in Economy By DAVID WESSEL
> Wall Street Journal - April 21, 2005; Page A2

Past Presentations:

Presentation at the Magellan Center (Longmont) on 11/9/06:
Magellan Center "Big Idea" on Offshoring & "Trade", A Systems Thinking Perspective (pdf, 1085K)

Presentation to the Colorado Springs Manufacturing Task Force meeting on 5/5/05.

See the slides at this link: **A Systems Thinking Perspective on "Trade"** (pdf, 290K). **All**

This article (modified) appears in the Summer 2005 issue of the **Magellan Center**'s **Magellan Explorer** magazine with the

title: "**Is Our Trade Deficit Sustainable: A systems Thinking Perspective on Trade**" (pdf, 32K) ... in approximately the same format as in the magazine.

[Discussion below updated 4/25/06 & 5/4/06, including additional diagrams and charts. See update of charts on trade and jobs as of 3/07 at Populism, 'Trade' and Jobs].

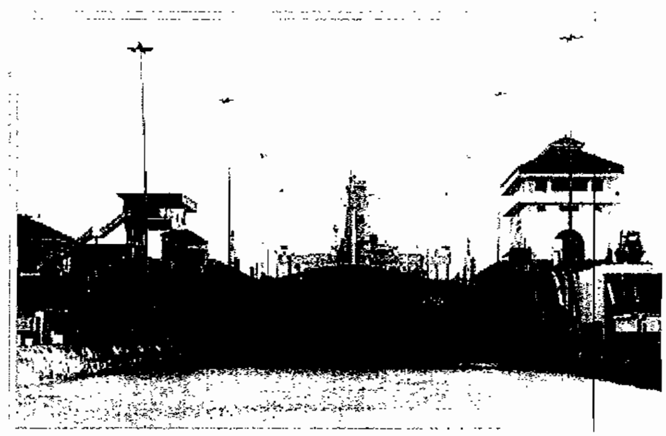
Top of Page

Exhibit Z18
Part 1

Balance of trade

From Wikipedia, the free encyclopedia

The **balance of trade** (or *net exports*, sometimes symbolized as *NX*) is the difference between the monetary value of exports and imports of output in an economy over a certain period. It is the relationship between a nation's imports and exports.[1] A favourable balance of trade is known as a **trade surplus** and consists of exporting more than is imported; an unfavourable balance of trade is known as a **trade deficit** or, informally, a trade gap. The balance of trade is sometimes divided into a goods and a services balance.



The balance of trade encompasses the activity of exports and imports, like the work of this cargo ship going through the Panama Canal.

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Definition

The balance of trade forms part of the current account, which includes other transactions such as income from the international investment position as well as international aid. If the current account is in surplus, the country's net international asset position increases correspondingly. Equally, a deficit decreases the net international asset position.

The trade balance is identical to the difference between a country's output and its domestic demand (the difference between what goods a country produces and how many goods it buys from abroad; this does not include money re-spent on foreign stocks, nor does it factor the concept of importing goods to produce for the domestic market).

Measuring the balance of trade can be problematic because of problems with recording and collecting data. As an illustration of this problem, when official data for all the world's countries are added up, exports exceed imports by a few percent; it appears the world is running a positive balance of trade with itself. This cannot be true, because all transactions involve an equal credit or debit in the account of each nation. The discrepancy is widely believed to be explained by transactions intended to launder money or evade taxes, smuggling and other visibility problems. However, especially for developed countries, accuracy is likely.

Factors that can affect the balance of trade figures include:

- Prices of goods manufactured at home (influenced by the responsiveness of supply)
- Exchange rates regarded in 1933
- Trade agreements or barriers
- Offset agreements
- Other tax, tariff and trade measures
- Business cycle at home or abroad.

The balance of trade is likely to differ across the business cycle. In export led growth (such as oil and early industrial goods), the balance of trade will improve during an economic expansion. However, with domestic demand led growth (as in the United States and Australia) the trade balance will worsen at the same stage in the business cycle.

Since the mid 1980s, United States has had a growing deficit in tradeable goods, especially with Asian nations (China and Japan) which now hold large sums of U.S debt that has funded the consumption.[2][3] The U.S. has a trade surplus with nations such as Australia and Canada. The issue of trade deficits can be complex. Trade deficits generated in tradeable goods such as manufaetured goods or software may impact domestic employment to different degrees than trade deficits in raw materials.

Economies such as Canada, Japan, and Germany which have savings surpluses, typically run trade surpluses. China, a high growth economy, has tended to run trade surpluses. A higher savings rate generally corresponds to a trade surplus. Correspondingly, the United States with its lower savings rate has tended to run high trade deficits, especially with Asian nations.

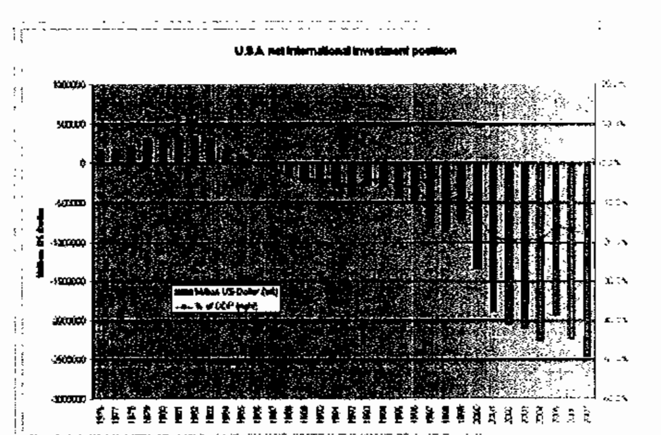
Views on economic impact

Economists are sometimes divided on the economic impact of the trade deficit.

Conditions where trade deficits may be considered harmful

Those who ignore the effects of long run trade deficits may be confusing David Ricardo's principle of comparative advantage with Adam Smith's principle of absolute advantage, specifically ignoring that latter. The economist Paul Craig Roberts notes that the comparative advantage principles developed by David Ricardo do not hold where the factors of production are internationally mobile.[4][5] Global labor arbitrage, a phenomenon described by economist Stephen S. Roach, where one country exploits the cheap labor of another, would be a case of absolute advantage that is not mutually beneficial.[6][7][8]

Since the stagflation of the 1970s, the U.S. economy has been characterized by slower GDP growth. In 1985, the U.S. began its growing trade deficit with China. Over the long run, nations with trade surpluses tend also to have a savings surplus while the U.S. has been plagued by persistently lower savings rates than its trading partners which tend to have trade surpluses with the U.S. Germany, France, Japan, and Canada have maintained higher savings rates than the U.S. over the long run.[9] Some economists believe that GDP and employment can be dragged down by an over-large deficit over the long run.[10][11] Wealth-producing primary sector jobs in the U.S. such as those in manufacturing and



Detiorating U.S. net international investment position (NIIP) has caused concern among economists over the effects of

computer software have often been replaced by much lower paying wealth-consuming jobs such those in retail and government in the service sector outsourcing and high U.S. trade deficits over the long-run.[2] when the economy recovered from recessions.[12][13][5] Some economists contend that the U.S. is borrowing to fund consumption of imports while accumulatiing unsustainable amounts of debt.[2][14]

In 2006, the primary economic concerns centered around: high national debt ($9 trillion), high non-bank corporate debt ($9 trillion), high mortgage debt ($9 trillion), high financial institution debt ($12 trillion), high unfunded Medicare liability ($30 trillion), high unfunded Social Security liability ($12 trillion), high external debt (amount owed to foreign lenders) and a serious deterioration in the United States net international investment position (NIIP) (-24% of GDP),[2] high trade deficits, and a rise in illegal immigration.[15][14]

These issues have raised concerns among economists and unfunded liabilities were mentioned as a serious problem facing the United States in the President's 2006 State of the Union address.[16][15] On June 26 2009, Jeff Immelt, the CEO of General Electric, called for the United States to increase its manufacturing base employment to 20% of the workforce, commenting that the U.S. has outsourced too much in some areas and can no longer rely on the financial sector and consumer spending to drive demand.[17]

Conditions where trade deficits may not be harmful

When economists contend trade deficits are not harmful, they generally refer to explanations of comparative advantage. Buyers in the receiving country send the money back. A firm in America sends dollars for Brazilian sugarcane, and the Brazilian receivers use the money to buy stock in an American company. This may lead to profits leaving the U.S however as Americans may forfeit control. Although this is a form of capital account reinvestment, it may not be a liability on anyone in America.

Such payments to foreigners have intergenerational effects: by shifting the consumption schedule over time, some generations may gain and others lose [18]. However, a trade deficit may incur consumption in the future if it is financed by profitable domestic investment, in excess of that paid on the net foreign debts. Similarly, an excess on the current account shifts consumption to future generations, unless it raises the value of the currency, detering foreign investment.

However, trade inequalities are not natural given differences in productivity and consumption preferences. Trade deficits have often been associated with international competitiveness. Trade surpluses have been associated with policies that skew a country's activity towards externalities, resulting in lower standards. An example of an economy which has had a positive balance of trade was Japan in the 1990s.

Milton Friedman argued that trade deficits are not necessarily important as high exports raise the value of the currency, reducing aforementioned exports, and vise versa for imports, thus naturally removing trade deficits not due to investment. Milton Friedman's son, David D. Friedman, shares this view and cites the comparative advantage concepts of David Ricardo.[19]

Milton Friedman on trade deficits

In the 1980s, Milton Friedman, the Nobel Prize-winning economist and father of Monetarism, contended that some of the concerns of trade deficits are unfair criticisms in an attempt to push macroeconomic policies favorable to exporting industries. In the late 1970s and early 1980s, the U.S. had experienced high inflation and Friedman's policy positions tended to defend the stronger dollar at that time. He stated his belief that these trade deficits were not necessarily harmful to the economy at the time since the currency comes back to the country (country A sells to country B, country B sells to country C who buys from country A, but the trade deficit only includes A and B). However, it may be in one form or another including the possible tradeoff of foreign control of assets. In his view, the "worst case scenario" of the currency never returning to the country of origin was actually the best possible outcome: the country actually purchased its goods by exchanging them for pieces of

cheaply-made paper. As Friedman put it, this would be the same result as if the exporting country burned the dollars it earned, never returning it to market circulation.[20] This position is a more refined version of the theorem first discovered by David Hume.[21] Hume argued that England could not permanently gain from exports, because hoarding gold (i.e., currency) would make gold more plentiful in England; therefore, the prices of English goods would rise, making them less attractive exports and making foreign goods more attractive imports. In this way, countries' trade balances would balance out.[22]

Friedman believed that deficits would be corrected by free markets as floating currency rates rise or fall with time to encourage or discourage imports in favor of the exports, reversing again in favor of imports as the currency gains strength. In the real world, a potential difficulty is that currency markets are far from a free market, with government and central banks being major players, and this is unlikely to change within the foreseeable future. Nevertheless, recent developments have shown that the global economy is undergoing a fundamental shift. For many years the U.S. has bore world has lent and sold. However, as Friedman predicted, this paradigm appears to be changing.

As of October 2007, the U.S. dollar weakened against the euro, British pound, and many other currencies. For instance, the euro hit $1.42 in October 2007[23], the strongest it has been since its birth in 1999. Against this backdrop, American exporters are finding quite favorable overseas markets for their products and U.S. consumers are responding to their general housing slowdown by slowing their spending. Furthermore, China, the Middle East, central Europe and Africa are absorbing more of the world's imports which in the end may result in a world economy that is more evenly balanced. All of this could well add up to a major readjustment of the U.S. trade deficit, which as a percentage of GDP, began in 1991.[24]

Friedman and other economists have pointed out that a large trade deficit (importation of goods) signals that the country's currency is strong and desirable. To Friedman, a trade deficit simply meant that consumers had opportunity to purchase and enjoy more goods at lower prices; conversely, a trade surplus implied that a country was exporting goods its own citizens did not get to consume or enjoy, while paying high prices for the goods they actually received.

Perhaps most significantly, Friedman contended strongly that the structure of the balance of payments was misleading. In an interview with Charlie Rose, he stated that "on the books" the US is a net borrower of funds, using those funds to pay for goods and services. He pointed to the income receipts and payments showing that the US pays almost the same amount as it receives: thus, U.S. citizens are paying lower prices than foreigners for capital assets to exchange roughly the same amount of income. The reasons why the U.S. (and UK) appear to earn a higher rate of return on their foreign assets than they pay on their foreign liabilities are not clearly understood. An important contributing factor is that the U.S. has investment primarily in stocks abroad, while foreigners have invested heavily in debt instruments, such as U.S. government bonds [25]. [26] Other reports contend that U.S. net foreign income has deteriorated, and appears set to stay in deficit in the future [27].

Friedman presented his analysis of the balance of trade in *Free to Choose*, widely considered his most significant popular work.

Warren Buffett on trade deficits

The successful American businessman and investor Warren Buffett was quoted in the Associated Press (January 20, 2006) as saying "The U.S trade deficit is a bigger threat to the domestic economy than either the federal budget deficit or consumer debt and could lead to political turmoil... Right now, the rest of the world owns $3 trillion more of us than we own of them."

John Maynard Keynes on the balance of trade

In the last few years of his life, John Maynard Keynes was much preoccupied with the question of balance in international trade. He was the leader of the British delegation to the United Nations Monetary and Financial

Conference in 1944 that established the Bretton Woods system of international currency management.

He was the principal author of a proposal—the so-called Keynes Plan—for an International Clearing Union. The two governing principles of the plan were that the problem of settling outstanding balances should be solved by 'creating' additional 'international money', and that debtor and creditor should be treated almost alike as disturbers of equilibrium. In the event, though, the plans were rejected, in part because *"American opinion was naturally reluctant to accept the principal of equality of treatment so novel in debtor-creditor relationships"*. [28]

His view, supported by many economists and commentators at the time, was that creditor nations may be just as responsible as debtor nations for disequilibrium in exchanges and that both should be under an obligation to bring trade back into a state of balance. Failure for them to do so could have serious consequences. In the words of Geoffrey Crowther, then editor of The Economist, *"If the economic relationships between nations are not, by one means or another, brought fairly close to balance, then there is no set of financial arrangements that can rescue the world from the impoverishing results of chaos."* [29]

These ideas were informed by events prior to the Great Depression when—in the opinion of Keynes and others—international lending, primarily by the United States, exceeded the capacity of sound investment and so got diverted into non-productive and speculative uses, which in turn invited default and a sudden stop to the process of lending. [30]

Influenced by Keynes, economics texts in the immediate post-war period put a significant emphasis on balance in trade. For example, the second edition of the popular introductory textbook, *An Outline of Money*, [31] devoted the last three of its ten chapters to questions of foreign exchange management and in particular the 'problem of balance'. However, in more recent years, since the end of the Bretton Woods system in 1971, with the increasing influence of Monetarist schools of thought in the 1980s, and particularly in the face of large sustained trade imbalances, these concerns—and particularly concerns about the destabilising affects of large trade surpluses—have largely disappeared from mainstream economics discourse [32] and Keynes' insights have slipped from view [33], they are receiving some attention again in the wake of the financial crisis of 2007–2009. [34]

Physical balance of trade

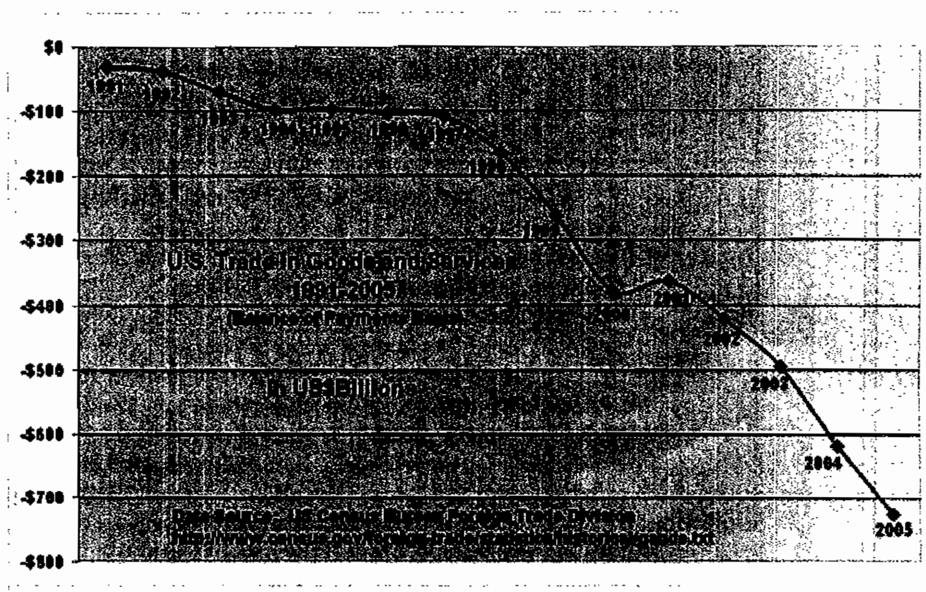
Monetary balance of trade is different from physical balance of trade (which is expressed in amount of raw materials). Developed countries usually import a lot of primary raw materials from developing countries at low prices. Often, these materials are then converted into finished products, and a significant amount of value is added. Although for instance the EU (as well as many other developed countries) has a balanced monetary balance of trade, its physical trade balance (especially with developing countries) is negative, meaning that a lot less material is exported rather than imported.

United States trade deficit

The United States of America has held a trade deficit starting late in the 1960s. It was this very deficit that forced the United States in 1971 off the gold standard. Its trade deficit has been increasing at a large rate since 1997 [35] (See chart) and increased by 49.8 billion dollars between 2005 and 2006, setting a record high of 817.3 billion dollars, up from 767.5 billion dollars the previous year. [36]

It is worth noting on the graph that the deficit slackened during recessions and grew during periods of expansion. Also of note, many economists calculate trade deficits and/or current account deficits as a percentage of GDP. The US last had a trade surplus in 1991, a recession year. Every year there has been a major reduction

in economic growth, it is followed by a reduction in the US trade deficit.[24] The investor Warren Buffett has proposed a tool called Import Certificates as a solution to the United States' problem.[37]



United States trade deficit (1991-2005).

See also

- List of the largest trading partners of the United States
- Current account
- Balance of payments
- FRED (Federal Reserve Economic Data)
- List of countries by current account balance

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36. ^ FTD - Statistics - Country Data - U.S. Trade Balance with World (Seasonally Adjusted)
37. ^ http://www.berkshirehathaway.com/letters/growing.pdf

External links

- Are Trade Deficits a Drag on U.S. Economic Growth?
- Graph of Historical U.S. Net Export of Goods and Services
- Where Do U.S. Dollars Go When the United States Runs a Trade Deficit? from Dollars & Sense magazine
- The Economic Impact of a U.S. Slowdown on the Americas from the Center for Economic and Policy Research
- OECD Trade balance statistics
- U.S. Government Export Assistance

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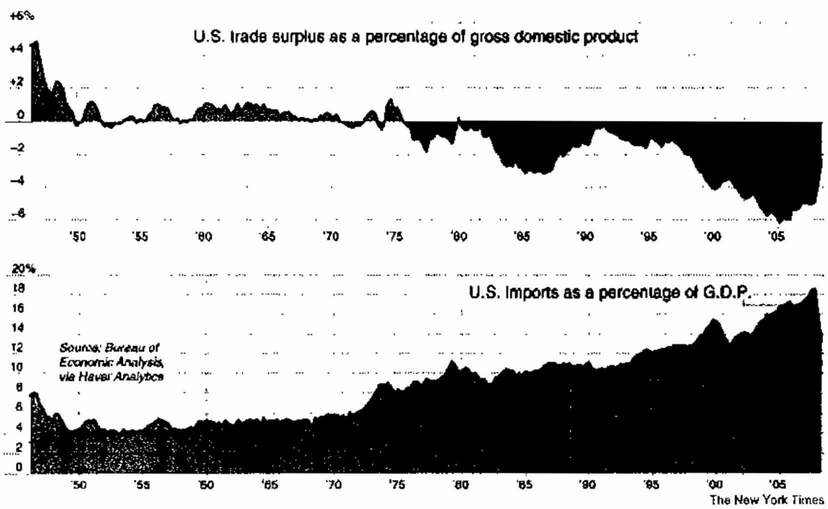
Categories: Macroeconomics | National accounts | Economic indicators | International trade | International economics | Economics terminology

Exhibit Z9 pg 4

OFF THE CHARTS

A Shrinking Trade Deficit, at Least for Now



By FLOYD NORRIS
Published: May 1, 2009

THE American trade deficit is collapsing at the fastest rate ever, a testament to the ability of a worldwide recession to sharply reduce global economic imbalances that had grown to unprecedented size.

The United States estimated this week that the trade deficit, as a percent of gross domestic product, fell to 2.4 percent in the first quarter of this year.

That is the smallest deficit in a decade, as can be seen in the accompanying chart. It is less than half of the deficit shown in the first quarter of 2008, when the American recession was new and not yet devastating other economies.

Few countries have reported first-quarter data as yet, and the American number will be revised. But what appears to be happening is that much of the pain from the fall in American consumption is being felt in other countries, since exporters in those countries supplied the products that Americans are no longer buying.

Declining trade deficits in the United States are likely to be matched by falling trade surpluses in countries that have historically been net exporters. That is one reason Germany's economy appears to be faltering badly and China has embarked on a huge

Exhibit Z9 pg5

- The Fallacy of Composition
- Trade Dynamics

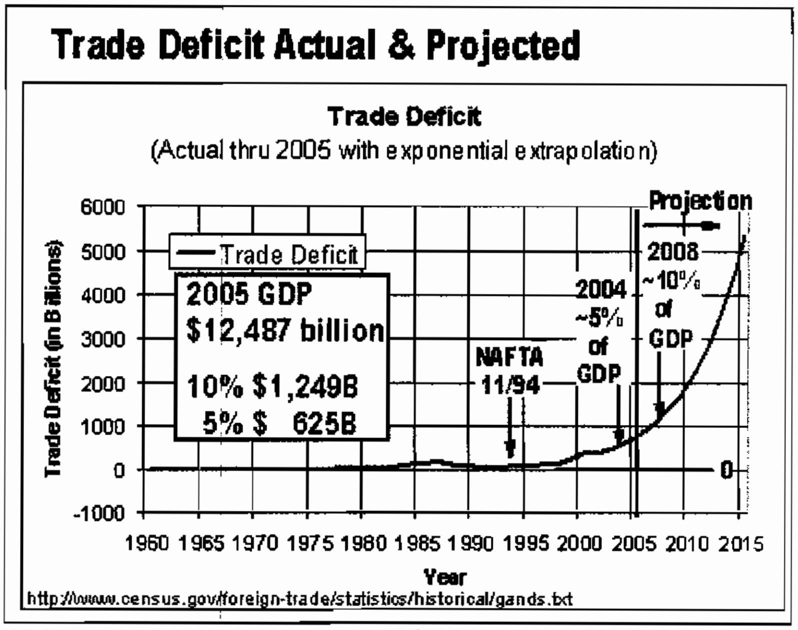
A preliminary on the greatly misunderstood concept of "comparative advantage"

It must be noted that the issue of "trade" and the "trade deficit" is about more than simple "trade." "Trade" is the "exchange of one thing for another," not the "transfer of the factors of production." Because of this, the logic of "comparative advantage" does not apply. This is an important point because "free trade" advocates rest their arguments on the premise that "comparative advantage" applies. It does not. Instead, "absolute advantage" applies.

In A Systems Thinking Perspective on Manufacturing & Trade Policy, I draw from the following sources to explain.

Lester Thurow in *The Future of Capitalism* (1996, pp. 69, 70) explains the "theory of comparative advantage" and describes the assumptions required for it to hold:

> "The classical theory of comparative advantage is often taught as if everyone benefits from trade. Technically that is not true. The total income of every country that takes advantage of comparative advantage grows, but there will be individuals within each country who lose. What the theory holds is that those who gain from international trade receive enough extra income from their activities that they could compensate those who lose when international trade commences. If that compensation isn't actually paid (and it almost never is), then those who lose are quite rational to oppose international trade.
>
> "But in the classical theory the losses usually will be quite small. First, full employment is assumed to exist. Free trade does not push anyone into unemployment. Second, transition costs are assumed to be zero. There is no region-, industry-, or firm-specific physical or human capital that is destroyed when workers are forced to shift between regions, industries, or firms. Third, returns are assumed to be everywhere equal. Each industry has the same rate of return on human or physical capital. Each firm and industry pays the same wage rate for a worker's being willing to give up an hour of leisure. As a consequence, being forced to shift jobs doesn't change wages very much, if at all."



U.S. Trade Deficit - actual with exponential projection

Paul Craig Roberts notes:

> "David Ricardo discovered the principle of comparative advantage in the early 19th century. He recognized that the principle did not hold if all factors of production are internationally mobile. Mobile factors of production would migrate to countries that had the greatest absolute advantages. Those countries would gain and all others would lose. ... Today, absolute advantage resides in an abundant supply of cheap and willing labor."

What's happening?

The chart above shows that the trade deficit for 2004, stated as $617.7B, was over 5% of GDP. At that time, projecting along the exponentially-increasing trend (note the confidence in the trend being exponential based on the data was excellent: R-squared = 0.9685), the trade deficit was projected to be at 10% of GDP by 2008.

In line with this trend, the February 2005 deficit was $61.04B, a yearly rate of $732.5B, over 6% of GDP. The actual U.S. trade deficit for all of 2005 was right in line with the exponential trend at $723.6 billion.

Source: Continuous Improvement Associates
http://www.exponentialimprovement.com/cms/fallacy.shtml

Social Issues

The Trade Deficit and the Fallacy of Composition

By Bob Powell, 5/04/05

Use your browser to search for "Updated". Especially see the chart on when the GDP crosses the cumulative trade deficit in the "What's Happening" section below.

Go to the section describing the "Fallacy of Composition"

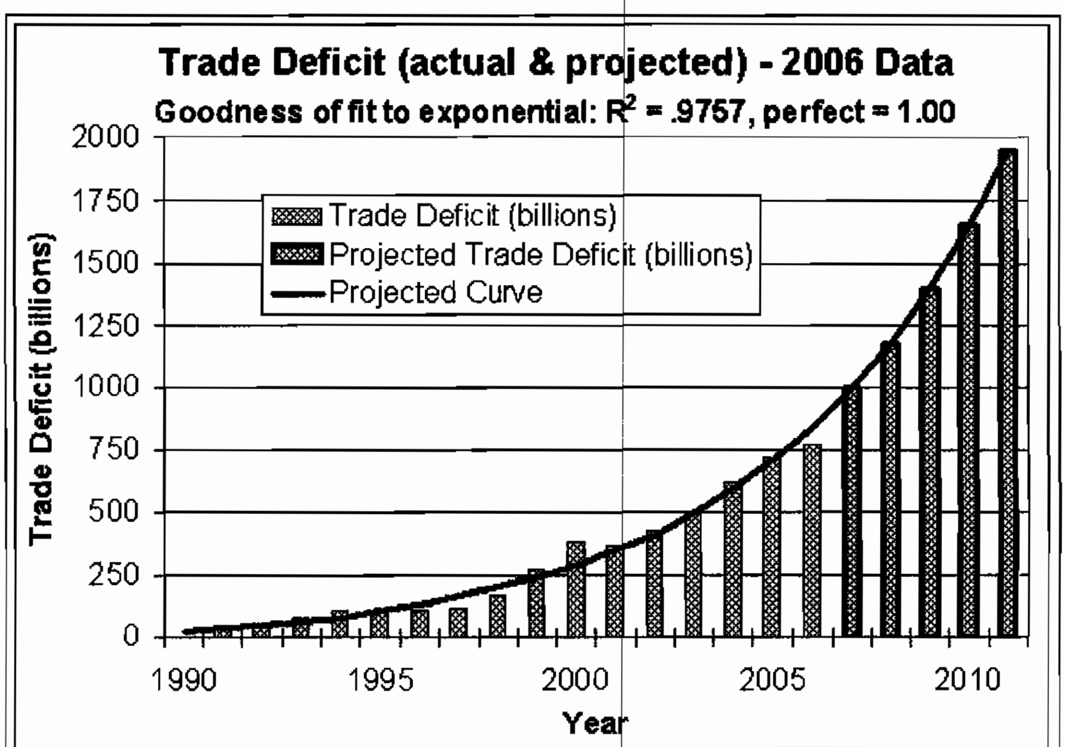
A presentation, "The Problem is Bigger than the Loss of Manufacturing" (Powerpoint, 1280K, links active in SlideShow mode, PDF w/links, 471K, PDF w/notes, 433K: Updated and expanded 8/28/07), contains updated charts on the U.S. 'trade' deficit and Colorado jobs through of July 2007 plus a summary of the main points on what to do about 'trade', taxes, and health insurance.

See also the very short handout on The Coming Economic Collapse from 'Trade' and Offshoring. 7/17/07.

Preface. The Impact of an Exponentially-Increasing Trade Deficit: We're Between a Rock and a Hard Place

The U.S. economy will collapse. Repeat. The U.S. economy, and probably the world economy, will collapse because of the United States' exponentially-increasing trade deficit.

Updated chart:



Trade Deficit thru 2006 with Trend: An excellent fit to an exponential function. Perfect fit = 1.000

That's overall and it's increasing rapidly with China, too. See the chart below.

The rest of the world will, within the next few years if not sooner (it's already happening), decide to stop taking U.S. dollars

Exhibit 29 A 6

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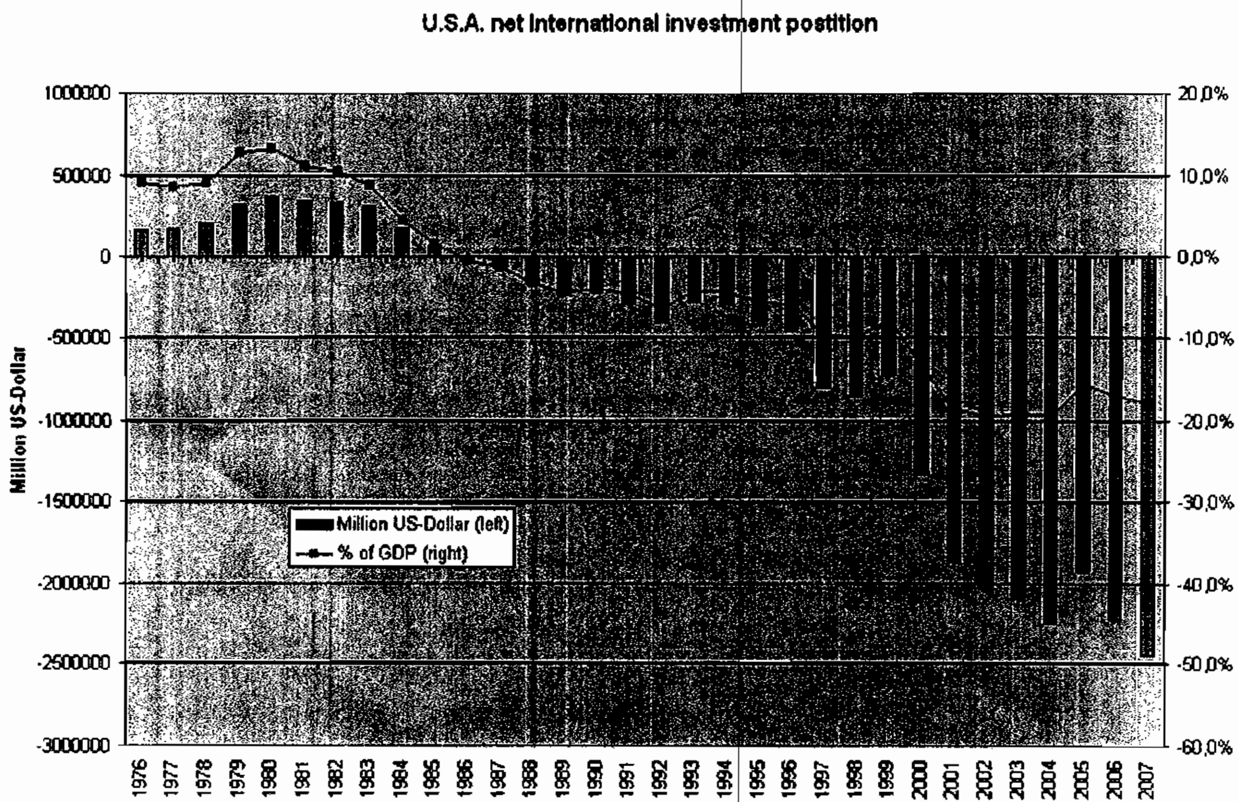

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Summary

Description	**English:** Net international investment Position of the United States '76 to '07.
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- Economy of the United States
- Rust Belt
- International international investment position
- Net international investment position

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Exhibit Z9 - pg 7

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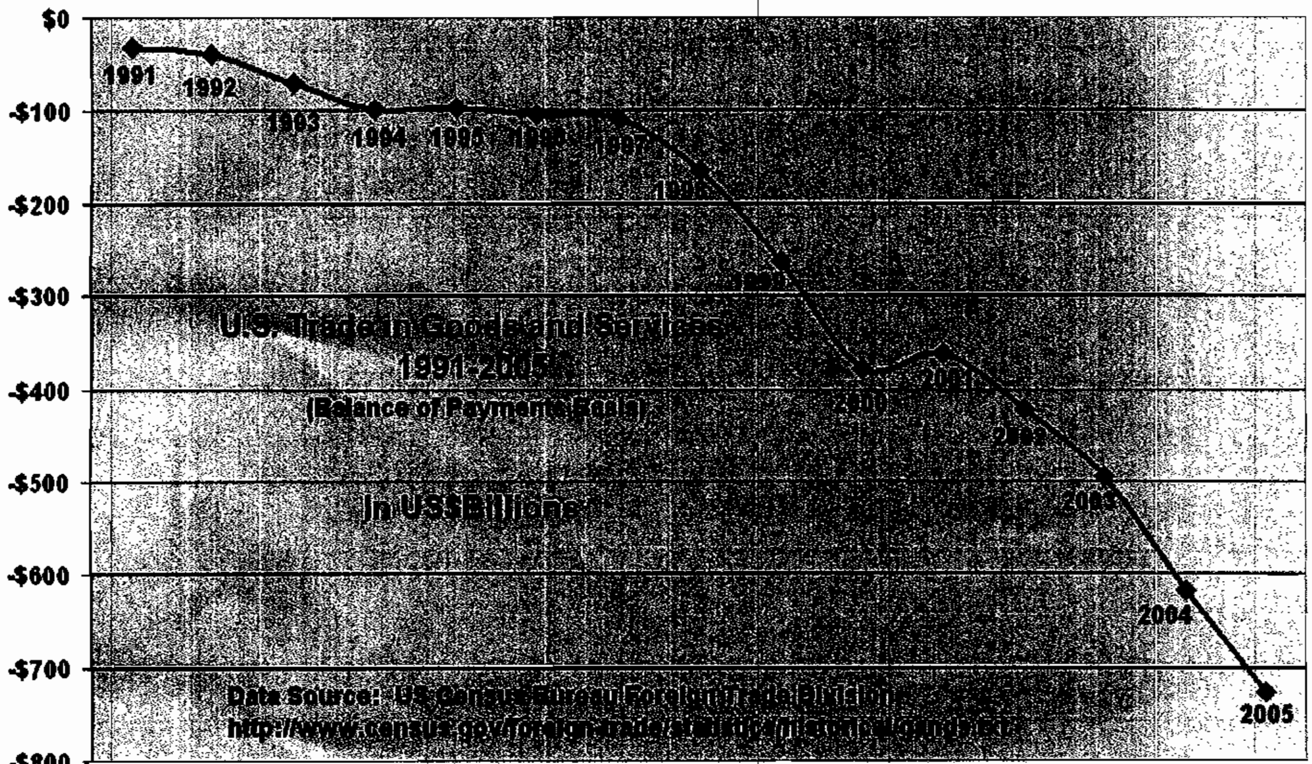

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Summary

A line chart showing the United States Balance of Trade, 1991 - 2005. Data Source: US Census Bureau Foreign Trade Division http://www.census.gov/foreign-trade/statistics/historical/gands.txt Line chart generated in a spreadsheet, then edited in GIMP. Data is US government data in the public domain. Chart is self-made and donated to the public domain. Chart created by Tom Cool (www.tomcool.us) (User:Tomcool) on 1 April 2006.

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	17:34, 1 April 2006	978×596 (53 KB)	Tomcool	(A line chart showing the United States Balance of Trade, 1991 - 2005. Data Source: US Census Bureau Foreign Trade Division http://www.census.gov/foreign-trade/statistics/historical/gands.txt Line chart generated in a spreadsheet, then edited in GIMP. Da)

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File links

The following pages on the English Wikipedia link to this file (pages on other projects are not listed):

- Balance of trade
- Chart
- User:Tomcool
- Line chart

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